

Recent Financial Developments

THE investment expansion that started about 5 years ago has continued in 1965. By the third quarter, gross private domestic investment was \$9 billion above the 1964 rate. Most of this advance was in nonresidential fixed investment, which increased through the first three quarters, continuing the steep rise that has been underway for a few years. Third quarter inventory accumulation, though down from the peak of the first quarter of 1965, was also above last year's pace. In contrast, outlays on residential structures were at about the same rate as they were in the middle of 1964, having fluctuated without any apparent trend since then. They are still a little below the peaks reached early last year. Net foreign investment was somewhat lower this year than last. The rise in private investment was matched by a rise in private saving from 1964 to the third quarter of this year. Undistributed corporate profits rose \$6 billion—mostly during the first half—and accounted for two-thirds of the advance. The corporate cash flow was augmented by a \$2½ billion advance in capital consumption allowances. Personal saving, which had been low during the first half, moved up sharply in the third quarter, to a volume about \$1 billion above the 1964 rate.

The difference between Federal receipts and expenditures on income and product account displayed a pattern just the opposite of that shown by personal saving. During the first half of 1965, the Federal Government showed a surplus averaging \$2½ billion (annual rate); during the third quarter, it ran a deficit of \$4 billion. To a large extent, these swings in personal saving and the budget position were closely related. Early in the year,

higher personal tax settlements on 1964 incomes boosted the Government surplus and held down the rise in disposable income and savings; in the third quarter, the cessation of these settlements and the retroactive Social Security payment tended to raise personal saving while increasing the Government deficit.

Contrast with earlier expansions

The investment expansion, together with increases in consumer purchases of autos and other durable goods, led to a marked rise in the demand for credit, which was largely accommodated at stable or slightly rising interest rates. This is in marked contrast to developments during previous periods of investment growth, for example, those of 1955-57 and 1959-60, when increased credit demands were accompanied by sharp increases in interest rates.

The comparative stability of interest rates during the economic advance that started in 1961 has reflected two major developments that differ from earlier experience: Corporate internal funds have advanced almost without interruption, and monetary policy has been more oriented toward keeping interest rates stable.

Corporate profits before taxes have risen almost every quarter during the past 5 years, whereas profits peaked rather early in previous expansions. The beneficial effects of this profit performance on internal funds were enhanced by the liberalization of tax depreciation regulations, by the tax credit on new investment, and by reductions in corporate tax rates. Although dividends were increased substantially over this period, internal funds rose \$24 billion from early 1961 through the summer of this year.

Over most of the current economic expansion, the rapid growth in corporate investment has lagged behind the rise in internal funds, corporation borrowing has been limited, and liquid assets have been well maintained. In contrast, earlier economic expansions were characterized by a rise in investment

CHART 7

Interest Rates

Long-term rates have moved up this year



U.S. Department of Commerce, Office of Business Economics

65-11-7

Table 1.—Sources and Uses of Funds, Nonfarm Nonfinancial Corporate Business, Annually, 1946-64

(Billions of dollars)

Line No.		1946	1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964
1	Sources, total.....	16.9	27.2	27.1	18.7	41.5	38.7	31.5	29.4	26.1	53.8	47.2	42.0	42.1	35.5	47.4	54.5	51.0	58.6	62.0
2	Internal sources ¹	7.8	12.5	10.7	18.1	17.9	19.9	21.2	21.1	23.9	29.2	28.9	30.4	29.5	35.0	34.4	28.5	41.4	44.3	49.4
3	Undistributed profits ¹	8.5	12.8	14.0	9.5	14.5	11.1	8.0	5.2	0.0	18.9	12.2	11.5	8.5	12.6	10.0	10.2	12.4	13.8	16.7
4	Corporate inventory valuation adjustment.....	-2.3	-0.9	-2.2	1.9	-5.0	-1.2	1.0	-1.8	-2.3	-1.7	-2.7	-1.5	-2.3	-1.5	-2.2	-1.1	-3.1	-4.4	-3.3
5	Capital consumption allowances ¹	4.6	0.7	8.8	7.8	8.6	10.0	11.2	12.9	14.6	17.0	15.4	20.8	21.4	22.0	24.2	25.4	29.3	31.0	32.9
6	External sources.....	9.1	14.4	8.5	-4.4	23.6	18.8	10.4	8.3	5.8	24.5	18.3	11.4	12.5	20.6	12.9	16.9	10.2	14.3	12.6
7	Stocks.....	1.1	1.2	1.9	1.3	1.4	1.9	2.3	1.8	1.0	1.0	2.3	2.4	2.1	2.2	1.0	2.6	0.6	-2.3	1.4
8	Bonds.....	1.0	2.4	4.3	2.9	1.0	3.3	4.7	3.4	8.4	2.8	2.0	6.9	4.7	3.0	3.4	4.6	4.6	8.9	4.0
9	Mortgages.....	0.8	0.9	0.3	0.6	1.0	0.2	0.5	0.3	0.7	0.7	0.4	0.9	1.2	1.2	0.7	1.7	2.0	2.6	3.4
10	Bank loans, n.s.f. ²	2.0	2.2	0.5	-1.6	2.6	3.8	1.7	-1.4	-1.0	3.4	4.8	1.3	-1.7	3.1	1.3	(*)	2.4	2.8	3.4
11	Other loans.....	(*)	1.1	0.3	0.9	1.2	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	1.0	0.3	0.7	0.5	1.3
12	Trade debt.....	0.1	2.7	0.8	-2.2	7.6	2.2	2.0	1.6	2.3	8.3	6.3	4.4	4.4	4.6	2.2	6.7	3.8	5.0	2.4
13	Profits tax liability.....	-1.9	2.3	0.9	-2.4	7.6	4.7	-2.3	3.0	-3.0	4.2	-2.0	-2.3	-2.3	2.2	-2.3	1.7	4.4	1.8	2.2
14	Other liabilities.....	2.1	1.3	0.3	0.8	1.5	2.5	2.2	1.8	3.0	3.9	3.9	2.4	2.1	2.8	2.9	2.4	3.8	1.9	2.5
15	Uses, total.....	31.7	30.7	28.1	14.3	45.4	35.9	27.6	35.3	28.9	50.7	44.9	49.7	40.9	52.5	47.6	52.1	56.0	60.6	64.5
16	Purchases of physical assets.....	17.5	18.7	19.8	14.0	22.2	23.4	23.4	30.5	29.7	35.0	33.8	33.8	29.5	35.1	36.7	34.9	42.6	43.6	49.5
17	Nonresidential fixed investment.....	10.9	14.8	17.2	14.8	15.8	20.1	20.6	29.3	21.4	24.0	29.7	32.6	27.5	29.2	32.6	31.1	34.3	38.7	41.3
18	Residential structures.....	7.6	3.9	2.6	0.9	6.4	3.3	2.8	1.1	1.7	1.0	5.3	1.2	1.8	1.7	1.2	3.8	3.0	2.7	3.7
19	Change in business inventories.....	6.0	1.2	2.1	-1.7	4.9	8.6	2.3	8.9	-1.9	4.9	4.9	0.6	-2.6	4.1	2.6	1.6	4.7	4.2	4.6
20	Increase in financial assets ²	4.1	14.0	5.3	4.4	21.2	7.4	4.1	2.7	5.3	21.8	9.9	6.8	14.4	17.7	5.8	17.2	34.6	16.9	14.9
21	Liquid assets.....	-4.6	1.1	1.1	3.2	4.4	3.0	0.3	1.9	-2.2	5.2	-4.2	-2.2	2.4	5.6	-4.1	3.3	2.4	3.0	0.6
22	Demand deposits and currency.....	1.1	2.2	0.3	1.1	1.6	1.8	0.8	0.8	2.1	1.0	0.2	(*)	-1.6	-1.0	-0.5	1.6	-2.3	-1.0	-2.8
23	Time deposits.....	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	1.3	1.9	3.7	3.9	3.2
24	U.S. Government securities.....	-5.3	-1.2	0.7	2.9	2.8	0.9	-1.7	1.5	-2.2	4.2	-4.5	-1.4	0.4	0.4	-5.4	-1.3	0.2	4.4	-1.6
25	Finance company paper.....	1.1	0.1	0.3	0.2	0.0	0.3	0.3	0.2	0.2	0.1	0.1	0.3	(*)	0.3	0.0	0.1	0.8	0.7	1.4
26	Consumer credit.....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
27	Trade credit.....	3.4	5.9	2.1	-1.8	10.2	1.5	3.5	1.7	4.7	10.9	7.6	3.0	2.5	5.9	0.3	0.4	7.8	8.0	8.0
28	Other financial assets.....	4.7	6.8	2.0	-1.5	8.7	1.7	-1.0	1.2	1.4	4.0	6.0	3.7	3.5	2.7	3.5	4.4	2.9	5.2	4.5
29	Discrepancy (uses less sources).....	4.6	3.5	-1.0	-4.4	1.9	-2.5	-4.0	-3.1	-2.3	-2.9	-2.3	-1.3	-1.3	-2.0	-4.8	-2.4	-5.0	-3.1	-3.5

Table 1.—Sources and Uses of Funds, Nonfarm Nonfinancial Corporate Business, Seasonally Adjusted Quarterly Totals at Annual Rates, 1957-60

(Billions of dollars)

Line No.		1957				1958				1959				1960			
		I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV
1	Sources, total.....	56.2	44.0	42.2	31.4	28.4	38.2	49.0	52.8	61.4	55.4	44.0	53.3	47.3	48.7	42.1	49.7
2	Internal sources ¹	36.4	36.0	31.1	23.9	26.9	27.8	36.1	33.1	34.1	35.5	34.1	35.2	26.0	35.2	34.1	32.4
3	Undistributed profits ¹	14.1	11.9	13.8	8.4	6.8	6.0	8.6	11.9	13.2	14.0	11.4	16.7	13.1	18.9	8.6	7.3
4	Corporate inventory valuation adjustment.....	-2.0	-1.1	-1.4	-0.7	-1.2	-1.7	(*)	-1.5	-1.0	-1.8	-0.5	-0.8	-1.3	0.1	1.0	0.9
5	Capital consumption allowances ¹	19.3	20.0	20.6	21.2	21.6	21.2	21.5	21.8	22.0	22.8	23.0	23.8	24.2	24.1	24.2	24.2
6	External sources.....	19.7	13.2	11.1	1.7	1.4	10.4	18.9	19.7	24.3	30.0	9.9	18.1	21.8	13.5	2.1	2.3
7	Stocks.....	3.0	2.7	1.2	1.9	1.0	3.0	1.9	1.8	2.1	2.1	1.2	2.5	1.5	2.0	1.8	1.0
8	Bonds.....	6.5	5.9	6.6	6.2	4.1	6.1	4.4	4.4	3.0	2.8	2.8	2.3	2.7	2.9	2.9	4.2
9	Mortgages.....	2.2	1.1	0.3	0.0	0.8	0.8	1.3	1.9	1.4	1.5	1.8	0.4	0.8	0.8	0.6	0.5
10	Bank loans, n.s.f. ²	2.6	2.5	0.5	-0.8	-2.5	-2.8	-2.2	2.2	1.7	4.6	4.1	2.1	5.0	1.0	-1.0	0.3
11	Other loans.....	1.0	0.5	0.0	1.2	1.2	-1.2	-1.8	0.4	2.2	0.8	0.7	-0.9	1.3	3.1	-1.4	0.8
12	Trade debt.....	4.6	1.1	0.0	-4.7	-1.4	8.0	6.4	3.7	7.4	5.4	-1.0	5.9	6.7	2.4	3.9	-4.4
13	Profits tax liability.....	-4.4	-3.2	-1.0	-3.4	-6.7	-5.0	4.4	2.1	4.9	7.1	-1.5	-1.7	-1.9	-3.4	-2.3	-3.3
14	Other liabilities.....	2.5	1.4	3.2	2.5	0.9	3.7	7.7	3.1	4.5	4.4	2.7	4.8	5.5	5.8	2.4	2.0
15	Uses, total.....	48.5	42.4	41.5	30.0	26.8	36.1	47.9	53.5	65.4	67.7	43.2	48.8	54.7	36.7	42.2	35.4
16	Purchases of physical assets.....	35.2	34.0	34.0	31.3	25.2	23.8	25.4	31.1	34.5	39.4	25.8	36.2	42.7	37.4	31.8	31.9
17	Nonresidential fixed investment.....	32.1	32.1	33.5	32.5	29.5	27.1	28.3	27.4	27.9	28.8	28.9	30.0	32.1	32.8	32.4	22.7
18	Residential structures.....	2.6	1.8	0.5	1.0	0.9	1.0	1.7	2.2	2.4	1.8	1.5	1.3	1.6	0.8	1.0	1.4
19	Change in business inventories.....	2.8	1.3	0.6	-2.2	-3.0	-4.5	-2.3	1.6	4.3	9.0	-1.6	4.9	10.1	3.9	0.5	-2.3
20	Increase in financial assets ²	13.3	4.7	6.8	-1.3	7.7	12.5	12.3	22.5	26.9	24.1	12.9	12.5	18.0	-7.7	2.3	3.5
21	Liquid assets.....	3.7	-1.0	-0.8	-1.9	-1.0	-0.3	3.1	3.9	5.7	8.4	7.7	-1.1	-3.0	-4.6	-3.7	-4.5
22	Demand deposits and currency.....	1.6	-1.5	(*)	-0.8	-2.2	1.0	3.0	1.5	-0.5	0.3	-2.1	-1.6	0.8	-0.6	0.7	-2.0
23	Time deposits.....	(*)	(*)	(*)	(*)	2.2	2.2	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4	(*)	2.0	0.5
24	U.S. Government securities.....	1.5	0.3	-1.7	-2.1	-3.8	-4.0	-7.7	5.8	6.7	5.6	0.6	1.4	-5.4	-4.1	-0.7	-0.5
25	Finance company paper.....	0.2	-0.1	0.2	1.0	0.3	-1.1	-1.1	(*)	-1.1	0.9	0.4	0.6	0.6	0.3	0.3	-0.3
26	Consumer credit.....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
27	Trade credit.....	3.4	3.6	2.8	0.3	-1.4	9.6	15.5	7.0	8.3	5.4	0.8	9.2	8.9	3.0	7.8	5.0
28	Other financial assets.....	3.6	8.7	4.5	1.1	2.7	2.2	2.8	0.5	2.7	4.4	2.8	2.9	4.5	-2.2	0.9	2.9
29	Discrepancy (uses less sources).....	-1.4	-1.3	-7.7	-1.7	-2.4	-2.1	-1.1	0.8	-3.0	-2.8	-0.8	-4.5	-8.1	-12.0	1.1	-5.2

Source: Board of Governors of the Federal Reserve System.

*Less than \$50 million.

¹ The figures shown here for "internal sources," "undistributed profits," and "capital consumption allowances" differ from those shown for "cash flow, net of dividends," "undistributed profits," and "capital consumption allowances" in the corporate gross product table (pages 42

Table 1.—Sources and Uses of Funds, Nonfinancial Nonfarm Corporate Business, Annually, 1952-56

(Billions of dollars)

1952				1953				1954				1955				1956				Line No.
I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	
32.4	22.4	34.0	37.3	35.0	35.4	29.7	29.6	32.8	23.9	31.0	32.6	44.9	48.0	62.7	62.2	45.7	45.4	47.5	49.3	1
20.9	20.3	20.1	22.3	22.7	21.4	21.2	19.3	21.4	22.0	23.5	25.6	28.6	29.4	28.0	29.7	24.8	26.6	29.4	29.0	2
10.6	7.4	8.7	0.1	11.4	10.1	10.6	4.0	7.0	8.6	9.0	10.1	13.0	13.3	14.2	14.3	12.7	13.3	12.4	12.3	3
5.6	1.8	1.1	1.5	7.7	1.2	2.7	7	8	1	7.8	1	1.4	1.6	2.5	2.4	2.2	3.1	1.4	2.0	4
10.8	11.1	11.3	11.7	13.0	12.6	13.1	13.7	13.9	14.3	14.8	16.4	16.1	16.7	17.4	17.8	18.3	18.4	18.4	18.7	5
10.6	2.1	11.9	16.0	12.3	14.0	5.5	1.3	1.6	1.0	7.5	13.1	23.1	16.6	23.6	32.6	17.0	16.8	18.1	21.3	6
2.2	2.0	1.4	2.8	2.1	2.3	1.3	1.0	3.0	2.0	0.6	0.8	2.5	0	1.3	3.2	2.1	1.0	2.3	2.7	7
4.7	6.3	6.1	3.0	3.9	3.3	2.6	4.2	3.8	3.3	0.8	1.7	2.2	2.3	2.1	4.8	2.1	3.7	4.7	4.0	8
6	4	4	6	4	3	1	3	2	7	1.0	1.0	1.0	1.0	1.0	1.1	1.1	1.1	1.1	1.1	9
2.6	1.9	1.8	3.0	4	(*)	6	-2.7	-1.3	-2.0	-7	1	1.2	3.1	4.6	4.7	4.4	4.3	3.7	4.2	10
2	2	3	1	4	3	0	-5	-1	-4	-3	-2	-3	3	-7	6	-4	3	5	-3	11
1.3	-2.6	6.4	4.4	4.6	1.2	-2.4	-8	-4	7	1.1	7.3	0.3	2.1	0.8	12.0	1.7	5.8	4.4	5.4	12
-3.5	-4.8	-2.0	-1.1	1.3	3.0	1.3	-4.1	-6.4	-3.0	-2.0	-6	4.8	5.1	3.1	2.8	-3.9	-3.4	-2.2	1.3	13
4.8	2.8	2.5	7	2.7	1.5	2.1	2.0	2.0	1.3	2.3	2.5	1.6	3.9	2.7	3.7	4.8	3.0	4.3	2.6	14
20.2	18.7	20.6	33.7	32.7	31.5	24.5	16.3	19.7	22.9	33.9	38.6	49.2	46.5	58.7	63.6	43.9	43.3	43.6	49.3	15
24.6	21.3	22.3	25.7	24.4	26.3	24.1	19.4	19.6	19.3	20.0	23.1	25.9	24.9	31.0	37.4	34.4	34.4	33.6	35.6	16
20.7	21.3	18.5	20.0	21.5	22.0	22.8	22.3	21.6	21.1	21.4	21.4	21.3	22.9	25.0	27.1	27.8	29.0	30.7	31.3	17
7	7	5	7	6	6	3	4	7	1.1	1.2	1.2	1.6	0	6	3	0	0	0	0	18
3.2	-7	2.4	4.1	2.3	2.0	1.0	-1.9	-2.6	-2.0	-2.7	4	2.1	1.4	5.4	0.8	0.3	4.8	4.0	3.0	19
2.7	-2.6	1.1	8.0	8.3	6.9	7	-1.2	-1	2.0	5.9	13.5	22.8	20.6	19.7	21.5	21.5	21.5	7.0	14.3	20
1.8	1	-4	-3	2.3	3.1	2.4	-2	-2.6	-2.0	3.0	1.3	9.3	6.8	5	4.1	-5.4	-5.0	-4.9	-5	21
4.1	-1.5	1.1	7	1.0	3.7	-1.0	-6	-1.0	3.6	3.1	2.0	5.5	-7	-4	-3	-4	-1.0	-0.6	2.3	22
(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	(*)	23
-2.5	0	-1.6	4	4.0	-4	2.8	-1	-1.6	-6.4	4	-1.4	4.1	0.8	1.2	4.6	-5.7	-5.0	-4.7	-2.0	24
2	7	-3	8	1	3	5	6	-1	-3	-1	-1	-3	7	-2	(*)	3	1	4	-3	25
3	1.2	7	8	3	3	2	2	3	2	2	4	3	6	6	7	5	1	6	3	26
2.1	-1.1	7.5	5.1	4.1	9	-2.0	-3.9	1.2	4.1	3.4	10.0	11.1	8.9	12.6	11.1	6.7	7.7	7.5	8.3	27
-1.6	-2.9	-1.1	2.3	1.5	7	1.9	4	1.0	1.3	1.9	1.7	3.8	4.2	5.8	5.3	7.4	6.9	3.4	4.2	28
-4.2	-3.7	-4.6	-3.5	-2.3	-3.9	-1.9	-4.3	-2.3	-1.7	-2.1	-1.9	-3.6	-2.5	-1.9	-3.7	-1.5	-2.1	-4.9	-4	29

Table 1.—Sources and Uses of Funds, Nonfinancial Nonfarm Corporate Business, Seasonally Adjusted Quarterly Totals at Annual Rates 1961-65

(Billions of dollars)

1961				1962				1963				1964				1965				Line No.
I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	
44.0	57.5	52.1	64.3	65.5	60.2	66.2	51.6	66.4	47.3	61.4	59.0	61.3	67.2	78.0	67.5	90.7	87.2			1
32.3	28.5	34.2	39.2	41.3	41.0	41.7	41.2	42.7	43.3	45.6	45.2	46.7	48.3	50.2	49.4	58.6	55.5			2
7.4	6.8	10.0	12.5	12.6	12.0	12.3	12.7	12.4	13.9	14.1	14.0	16.2	16.7	16.8	16.7	22.7	22.5			3
-1.1	5	-1.3	-2	-1	(*)	1	0	2	-0.9	2	-1.2	-4	(*)	2	-1.0	-1.4	-1.7			4
34.7	25.3	25.0	20.1	28.6	29.0	29.3	29.7	30.1	30.8	31.9	31.8	32.2	32.6	33.2	33.7	34.3	34.7			5
11.7	21.9	16.9	25.1	24.5	19.2	24.5	8.4	23.7	23.9	16.9	13.8	12.6	17.9	25.8	18.1	35.1	31.7			6
2.7	5.1	1.8	2	5	9	3	5	(*)	3	3	-1.6	2.0	3.3	1.1	-1.5	(*)	1.8			7
2.8	7.1	4.1	4.5	6.0	5.0	4.1	3.6	4.0	3.4	2.6	3.7	3.6	3.8	4.2	4.3	4.7	5.0			8
1.2	1.7	1.0	2.1	2.5	1.0	3.1	2.9	2.7	3.4	3.6	3.7	2.6	3.0	3.2	3.7	2.8	3.6			9
1	-2.3	1.3	0.9	1.1	2.6	3.3	2.6	1.4	2.6	1.9	5.4	-1.4	4.3	3.1	7.8	9.9	10.2			10
-0.9	1.4	0	-1.1	(*)	1.7	1.5	-1.3	1	1.2	7	-1	3	2.7	1.1	1.1	2	2.1			11
0.0	6.5	2.4	11.2	7.6	3.0	8.1	-3.0	10.0	0.6	3.5	0	3.2	-4.7	0.0	3.2	6.5	4.3			12
-1.2	1.9	2.3	3.8	6	3	1.1	-6	1.9	3.1	1.4	8	1	6	-1	9	3.8	-1.3			13
5	3	1.3	3.6	7.1	2.1	3.1	3.1	1.9	3.7	0	1.2	1.1	5.1	4.2	-1.0	4.7	4.2			14
41.5	56.4	49.7	62.0	68.5	58.6	61.5	47.4	62.3	63.8	60.5	66.1	63.1	62.6	74.0	63.2	85.7	81.3			15
30.5	31.8	38.3	38.9	42.2	42.5	43.4	40.7	42.2	42.4	44.1	45.7	47.3	48.0	45.6	54.4	54.5	55.5			16
30.0	30.3	31.3	32.2	32.5	34.2	34.1	34.2	34.5	35.1	36.0	37.1	38.7	40.0	41.0	43.8	40.5	40.7			17
1.8	2.1	2.4	2.7	2.7	3.2	3.3	2.9	3.5	3.8	3.7	3.9	4.0	3.8	3.6	3.6	4.2	4.2			18
-1.8	1.3	2.4	4.1	0.0	5.1	4.0	3.6	4.3	3.6	4.4	4.8	3.7	4.1	3.4	7.0	7.7	5.0			19
12.4	22.0	15.4	19.5	18.3	14.0	19.0	6.7	20.5	20.5	16.4	19.4	11.5	14.7	15.4	7.7	27.3	24.8			20
4.6	7.1	1.6	(*)	2.9	1.2	3.4	2.2	1	6.2	2.7	4.2	3	3.1	5.0	-8.5	-2.1	-1.7			21
5.6	3.5	1.8	1.2	-5.1	-3.1	5	-1.4	-6.9	2	-1.1	-8	-7.2	2.1	3.1	-7.5	-4.9	-4.3			22
5.8	1.4	2.2	-1.4	7.0	2.6	7	3.4	4.5	3.4	2.2	5.2	6.4	1.4	1.5	2.4	3.3	6.9			23
-1.8	2.2	-1.9	-4	9	2	-3	(*)	8	1.1	4	-8	2	-2.4	-2	-2.5	-1.5	-4.0			24
-1.4	(*)	(*)	-7	3	0	3.3	3	4	1.6	2	1.8	1.0	2.0	1.6	1.1	(*)	0			25
-3.2	1.1	1.2	1.3	3	1.5	9	1.5	10.5	1.6	9	5.5	2	1.7	9	1.0	1.7	4			26
0.4	12.1	5.7	13.5	9.8	8.5	11.5	1.8	13.5	8.9	8.5	6.0	6.7	5.6	14.4	9.0	14.2	12.4			27
6.3	2.4	3.0	5.0	3.3	2.8	3.2	2.2	10.3	4.7	0.2	-3	4.5	4.3	5.1	4.2	13.3	12.8			28
-0	-1.1	-2.4	-5.5	-7.3	-3.7	-4.8	-4.2	-3.4	-5.0	-3	-2.9	-2.3	-4.6	-2.9	-5.3	-1.1	-5.0			29

through 55 of the September 1965 Survey) for the following reasons: (1) these figures include, and the statistics in the corporate gross product table exclude, branch profits remitted from net of corresponding U.S. remittances to foreigners; and (2) these figures exclude, and the

corporate gross product figures include, the internal funds of corporations whose major activity is farming.
 * Includes some categories not shown separately.

outlays greater than the rise in internal funds, by relatively heavy corporate borrowing, and by reductions in holdings of liquid assets.

Generally speaking, monetary policy since 1961 has been oriented toward providing sufficient funds to finance the rise in business activity; during earlier economic advances, there were shifts to tight money after the initial recovery periods. The current business advance has been marked by record expansions in bank credit, whereas during earlier economic rises the volume of new bank credit declined.

During the past 9 months, however, there has been some reversion to past patterns: The growth of corporate investment outstripped the rise in internal funds; corporate borrowing increased, and since late last year, monetary policy has been somewhat less easy.

Monetary policy moves away from ease

A moderate increase in pressure on bank reserve positions has been apparent this year. Although the volume of bank credit supplied so far in 1965 has been 22 percent above the 1964 rate, new credit, though substantial, has declined from the very high first quarter peak.

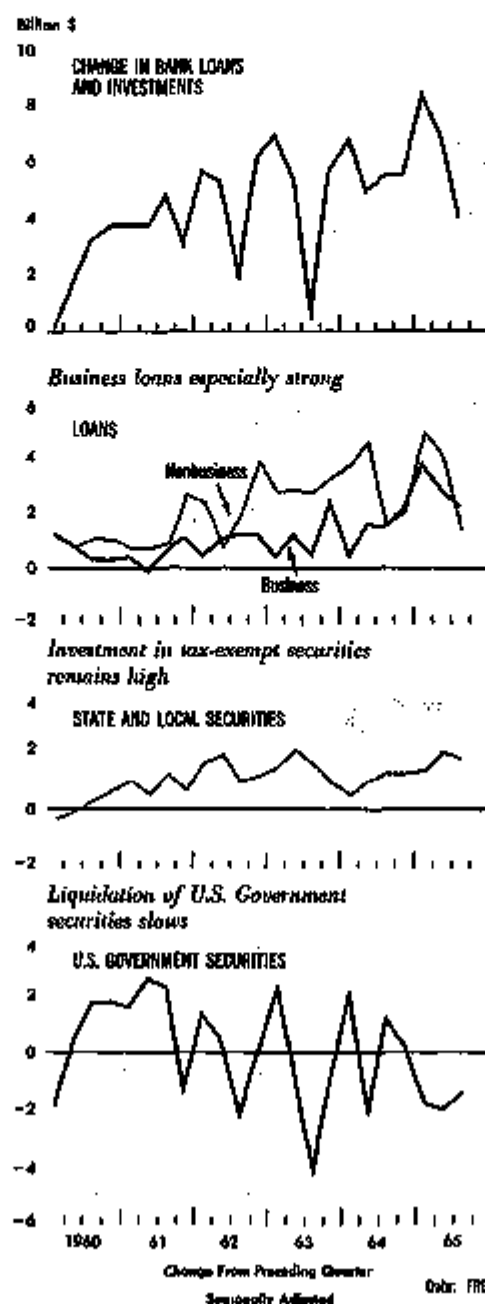
The change in monetary policy has permitted bank reserves to expand, but not enough to match the increase in total credit. Although Federal Reserve purchases of U.S. Government securities through September were over \$2 billion as compared with less than \$1½ billion in the corresponding period of 1964, a \$1½ billion decline in the gold stock and a \$½ billion increase in currency in circulation absorbed the funds supplied by the open-market purchases. Borrowed reserves have risen throughout the year and by September had reached \$627 million, the highest since the end of 1959.

As compared with last year, business loans have expanded very sharply in 1965: The \$11½ billion increase this year (seasonally adjusted annual rate) was almost twice the increase in all of 1964. The rate of advance slowed after the adoption of voluntary guidelines on foreign lending early in the year and as steel inventory accumulation by steel

users slackened after the threat of a steel strike disappeared. Lending to consumers in 1965 has outpaced last year's rate by a wide margin: \$4½ billion as compared with \$2½ billion. Purchases of State and local securities at \$6½ billion have been 80 percent above the 1964 pace. Real estate loans increased almost \$5 billion, slightly above the previous year's rate.

Bank Credit

Total credit creation still high but off from first quarter peak



U.S. Department of Commerce, Office of Business Economics

16-11-5

As banks have met the enlarged demands of their customers for credit accommodation, bank holdings of U.S. Government securities have been reduced by almost \$7 billion so far in 1965, as compared with a decline of less than \$1 billion in 1964. In recent months, the slackening in business loan demands and a decline in bank investment in tax-exempt securities have been reflected in a modest restoration of bank holdings of U.S. Government securities.

Corporation investment up

Corporate fixed and inventory investment has risen sharply this year. As noted earlier, the increased investment requirements have outstripped the rise in internal funds, and corporations have increased their borrowing.

Fixed investment expenditures this year have risen more than \$5 billion at annual rates above the 1964 pace and reached \$53 billion at seasonally adjusted annual rates by the third quarter. Manufacturers of both durable and nondurable goods have been responsible for an unusually large part of the increase. In contrast, investment by corporations in apartment houses has shown little increase from the rate of the last 2 years.

Corporations have added about \$6 billion (at annual rate) to their inventories so far in 1965; this compares with an increase of \$4½ billion in 1964. The rate of accumulation was highest in the first quarter and has since moderated.

Direct investment abroad by U.S. corporations rose in the first half of 1965 to an annual rate of over \$4 billion. It is expected that there will be a lower rate of outflow in the second half of the year.

Corporate before-tax profits have risen sharply again this year. The second phase of the reduction of Federal taxes has also increased after-tax profits. Since dividend payments, though high, have grown little so far this year, retained earnings have continued to expand, and so have capital consumption allowances. These factors combined have increased total internal funds by \$6 billion over 1964. Because of the faster growth in investment,

corporations have sharply increased their borrowing. Early in the year, bank loans amounted to about \$10 billion at annual rates, but they have since fallen as inventory accumulation has declined.

Bond issues by corporations have also been stepped up, reaching a pace of almost \$5½ billion (net of retirements) in the first 9 months of 1965, as compared with \$4 billion in 1964. On the other hand, stock issues, at under \$1 billion, have been about half of last year's total. Mortgage borrowing has been little changed from last year.

Liquid assets declined \$2 billion in the first half. The decline affected mainly U.S. Government security holdings: Cash holdings—particularly time deposits—have been well maintained. The decline in holdings of liquid assets has brought corporate liquidity ratios to their lowest level since 1945.

Consumer finance

Consumers' investment patterns have apparently changed somewhat in 1965. Though total deposit accumulation has been about the same as last year, there has been an increased emphasis on bank time deposits and less on savings and loan shares. Purchases of corporate and tax-exempt bonds have moved up, and corporate stocks have been sold on balance. Although the stock market has been extremely active this year, evidence as to small investor participation is conflicting: Odd lot purchases have risen less than total transactions; mutual fund sales, however, have moved ahead of market transactions.

Consumer installment credit has continued to rise. New installment credit increased more than \$7½ billion at annual rates in the first 9 months of 1965 compared to \$5½ billion in 1964. The rise was concentrated in auto and personal loans.

Mortgage financing has climbed moderately from last year's pace. Although the number of homes sold was unchanged from last year, the rising price level of houses and selective increases in loan-to-value ratios have helped to raise new mortgage borrowing.

Government borrowing

Although there have been marked shifts in the Federal budgetary position

during 1965, they have had little direct impact on money and capital markets. The swing from surplus to deficit in the Federal Budget was not fully matched in Federal borrowing. During the first half of the year, net Federal debt outstanding fell by \$3½ billion, and debt fell further during the third quarter. The Federal Government built up its cash balances during the period of surplus and drew them down in the third quarter.

Treasury financing operations so far this year have been marked by a reliance on Treasury bills to raise cash. However, there has been a moderate lengthening of the average maturity of the public debt because of an advance refunding in January.

State and local governments stepped up their borrowing during the first 9 months to an \$11 billion annual rate, as compared with \$10½ billion in 1964. A substantial volume of these funds entered into liquid assets held by State and local governments, pending disbursement of the funds on public works.

Interest rates rise

The financial developments reviewed in this report have contributed to a moderate rise in most market interest rates this year. Short-term rates, which rose sharply in 1964, rose further early in the year and have since fluctuated around the levels reached then. After a long period of comparative stability, long-term yields moved up this summer.

In part, the different timing of movements in interest rates reflected different timing in demands for funds: Inventory buying and associated short-term fund demands were especially large early in the year, whereas corporate bond issues were highest in the summer.

However, expectations also played a substantial role, particularly in the summer rise in long-term rates. After the enlargement of U.S. military participation in Vietnam during the summer, there were widespread expectations that credit demands—already large because of the business expansion—would rise even more. In recent weeks, the rise in market interest rates has leveled off, as several Government

officials have indicated that prospective economic developments did not require higher interest rates.

Note on Revised Statistics on the Sources and Uses of Corporate Funds

Recent changes in definitions used in the National Income and Product Accounts (prepared by the Office of Business Economics) and in the Flow of Funds Accounts (prepared by the Board of Governors of the Federal Reserve System) have brought these two economic accounting systems into closer definitional agreement than they were in the past. A reconciliation of the two systems is published in the November 1965 issue of the *Federal Reserve Bulletin*.

The estimates in the Flow of Funds sector "nonfarm, nonfinancial corporations" are now conceptually equivalent to what OBE would publish for such a sector. OBE has therefore discontinued its previous series on the sources and uses of corporate funds. For the convenience of our readers, we present the Flow of Funds data for this sector in the sources and uses of funds format on the following two pages, annually from 1946 through 1964; and quarterly, seasonally adjusted at annual rates, from 1952 through the second quarter of 1965. In the future, these statistics will be published in the *Survey* as well as in the *Federal Reserve Bulletin*.

The Flow of Funds series has a somewhat narrower industrial composition than OBE's former statistics on the sources and uses of corporate funds. The Flow of Funds sector "nonfarm, nonfinancial corporations" excludes farms, security and commodity brokers and dealers, finance companies and other credit agencies other than banks, and open-end investment companies; all of these groups were formerly included in OBE's statistics for the non-financial sector.

The relation of these statistics to the national income and product data published in the August 1965 *Survey* is as follows: The items classified under "internal sources" represent the portion of

(Continued on page 24)

Financing and Sales of Foreign Affiliates of U.S. Firms

(Continued from page 19)

Table 7.—Sales of Mining Affiliates Abroad, by Area and Destination, 1957, 1963, and 1964
(Millions of dollars)

Area	Total sales			Local sales			Exported to United States			Exported to other countries		
	1957	1963	1964	1957	1963	1964	1957	1963	1964	1957	1963	1964
All areas, total.....	2,432	2,462	2,943	325	322	323	838	862	1,084	609	1,008	1,296
Canada.....	248	1,008	1,250	124	286	335	490	466	660	216	390	354
Latin America, total.....	920	963	1,200	104	132	200	483	452	460	413	339	644
Mexico, Central America, and West Indies.....	223	223	339	67	80	180	112	123	74	44	20	68
South America.....	586	620	831	37	41	195	225	227	246	323	352	400
Other Western Hemisphere.....	111	120	140	(*)	1	1	63	102	120	46	17	10
Europe.....	70	60	80	16	10	10	4	2	(*)	48	38	40
Africa.....	238	286	330	46	4	3	77	37	65	112	244	260
Asia and Oceania.....	66	104	133	31	63	69	14	6	9	30	37	55

Note.—Details may not add to totals because of rounding, and 1964.

* Less than \$600,000.

† West Indies excludes Cuba in 1963

latest data showing the coverages of the samples used and a reconciliation with data collected for use in the balance of payments accounts.

Table I updates figures on the exploration and development expenditures of foreign affiliates charged against their income accounts. These figures can be used in conjunction with the data on plant and equipment expenditures given in this article and in the Survey for September 1965 to provide a more complete picture of foreign investment activity by U.S. firms.

Sales of Foreign Manufacturing Affiliates, by Area, 1964
(Millions of dollars)

Area	Reported data	Estimated total	Percent reported
All areas.....	23,811	37,278	79
Canada.....	8,586	11,450	75
Latin America.....	3,876	8,100	78
Europe.....	13,807	18,500	84
Other areas.....	3,259	4,228	77

Plant and Equipment Expenditures of Foreign Affiliates, by Industry, 1964

(Millions of dollars)			
Industry	Reported data	Estimated total	Percent reported
All industries.....	4,870	9,118	81
Mining and smelting.....	343	430	81
Petroleum.....	1,876	2,084	91
Manufacturing.....	2,311	2,983	77
Trade.....	316	328	96
Other industries.....	234	321	70

Reconciliation of Data on Capital Flows and Earnings by Industry, 1964
(Millions of dollars)

Data on capital flows and earnings	Total, special industries	Mining and smelting	Petroleum	Manufacturing
Net capital outflow appearing in balance of payments accounts.....	1,824	39	739	990
Less:				
Purchases of existing enterprises and minority interests.....	349	2	13	336
Retained branch profits.....	307	100	1	0
Plus:				
U.S. financing, other than parent.....	48	-47	-2	97
Other adjustments and residual.....	49	19	18	11
Equals:				
Net funds from U.S. (table 1).....	1,466	-41	736	762
Undistributed earnings of subsidiaries consistent with balance of payments accounting.....	967	102	-49	814
Plus:				
Undistributed earnings of minority interests.....	274	131	3	140
Retained branch profits.....	107	100	1	0
Other adjustments and residual.....	118	-48	63	111
Equals:				
Retained earnings as derived from table 1.....	1,463	286	7	1,171

† Includes sales to foreigners of equity interests in existing affiliates.

Although the average level of prices was greater in the third quarter than in the second, the advance was very small, and indeed since late spring, the overall level of consumer prices has been quite steady.

The unusual spurt in prices this spring reflected mainly a sharp advance in food prices, particularly for meats, fruits, and vegetables; prices of these commodities have eased somewhat since early summer.

Prices of nonfood commodities, which had been fairly stable through most of 1964, rose an average of one-half of 1 percent in each of the first two quarters of this year but fell back somewhat in the third quarter. In household durables and new cars, part of the summer decline resulted from the excise tax reduction. Since the tax cuts, seasonally adjusted prices of household durable goods have edged down further, while new car prices (through September, just before the introduction of the 1966 models) have shown no significant change, after allowance for the usual seasonal influences. Used car prices, which rose contrasessionally at the time of the auto strikes early last winter, have weakened steadily this year and are now below the level of a year earlier.

Prices of consumer services have continued to increase about as much as in recent years. Prices of transportation, medical, and "other" services have risen a little more than the average for all services, and household services (excluding rent) somewhat less.

Recent Financial Developments

(Continued from page 18)

such items in table 11 of the August Survey which accrue to the nonfarm, nonfinancial group of corporations; the items classified under "increase in physical assets" represent the portion of those of "gross private domestic investment" (tables I and II of the August 1965 Survey) which was purchased by this group of corporations.

OBE is presently preparing a broad industrial breakdown of the sources and uses of funds of nonfarm, nonfinancial corporations.

Price Changes

(Continued from page 6)

Uptrend in CPI continues

From the first to the second quarter of 1965, the Consumer Price Index rose about $\frac{1}{2}$ of 1 percent after seasonal adjustment, about double the average quarterly rise of the preceding year.